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IN THE

Supreme Court of the United States

OCTOBER TERM, 1942.

Nos. 37-38

In the Matter of
CHICAGO AND NORTH WESTERN RAILWAY CO.,
Debtor,
LOUIS SUSMAN, et al., Convertible Bond Owners,
Petitioners,

VS.

MUTUAL SAVINGS BANK GROUP COMMITTEE, ET AL.,
Respondents.

On Petition for Writs of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

PETITION FOR REHEARING.

MEYER ABRAMS,
Counsel for Louis Susman, et al., Convertible Bond Owners, Petitioners.

SHULMAN, SHULMAN & ABRAMS, and
NORMAN ASHER,
134 N. LaSalle Street,
Chicago, Illinois,
Of Counsel.

May 10, 1943.

Midwest Law Printing Co., 340 W. Huron St., Chicago

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On Petition for Writs of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

PETITION OF LOUIS SUSMAN, ET AL., CONVERTIBLE BOND OWNERS, FOR REHEARING.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petitioners, Louis Susman, *et al.*, convertible bond owners herein, apply to this Court for rehearing from the order entered April 19, 1943, denying the prayer for writs of certiorari, and in support of the petition for rehearing, say:

Petitioners presented two issues of fact to the District Court which were never presented to the Interstate Commerce Commission, and on which it had no opportunity to pass because the petitioners were not parties to the hearings before the Commission prior to the adoption of the plan of reorganization. Petitioners did not know these facts at the time of the Interstate Commerce Commission hearings, and did not discover them until after the plan had been approved and presented to the District Court for confirmation. The issues are of great importance by reason of certain decisions which were published since the denial of the writs.

Under the ruling made by this Court in the Milwaukee Railroad reorganization (63 S. Ct. 727) such issues should have been presented to the Interstate Commerce Commission for its consideration. A rehearing should be granted so that the petitioners may have the opportunity to present them to the Commission. The issues are:

(a) whether the convertible bondholders were entitled to impress a trust on the $45,186,000.00 refunding bonds of the "Omaha," which were acquired by the debtor with funds supplied by the convertibles, and

(b) whether the convertible bonds which were entitled to 4¾% interest to the maturity of the loan and a bonus of 5% for retirement prior to maturity, were properly classified in the same class with general creditors who were not entitled to such rights.

This Court decided in the *"Milwaukee"* case (63 S. Ct. 727, 752) that *"minorities under §77 • • • cannot be deprived of the benefits of the statute by reason of a waiver, acquiescence, or approval by the other members of the class."* This rule should be applied to the instant case because the issues were never presented to the Interstate

Commerce Commission. One issue was presented to the District Court and considered in its opinion (35 F. Supp. 230, 254). However, this issue was not considered by the Circuit Court of Appeals. The other issue was not even considered by the District Court, and under the remandment order in the *Milwaukee* case, such issue should also be considered now.

In the "Milwaukee" opinion this Court remanded the case to the District Court with instructions to remand the case back to the Commission to determine certain facts with respect to the priorities between the general mortgage bonds and the 50-year bonds. The same rule should apply to the convertible bonds in the instant case, whose lien might be superior to that of other creditors on the bonds of $45,186,000.00 of the "Omaha," and also because of the preferential claim of the Convertibles over general creditors.

The rule of law announced in the *"Milwaukee"* case, that where senior creditors obtained the face value of their securities in inferior securities, they are entitled to additional securities for the surrender of their superior right, should apply with equal force in the instant case as it relates to their position as against the position of general creditors.

I.

The Right to Subrogation Or to Impress a Trust on the Refunding Bonds of the "Omaha" of $45,186,000.00 Should Be Considered By the Interstate Commerce Commission, and Should Have Been Squarely Passed Upon By the Court of Appeals, and a Rehearing Should Be Granted on This Issue.

The "Omaha," a wholly owned subsidiary of the debtor, was indebted on various liens for $45,186,000.00.

Its parent, the debtor, caused the "Omaha" to execute, on May 1, 1929, a "refunding" bond issue secured by a trust indenture which was to become a first lien upon the "exchange" of the "refunding bonds" for the existing bonds and the release of the existing liens. After the execution of the trust indenture, but before it obtained authority to issue the refunding bonds from the Commission, the debtor sold $72,335,000.00 of the Convertible bond issue to the public and *used* $45,186,000.00 *of the proceeds realized from the sale of these bonds to discharge the existing liens on the Omaha Railroad, but did not exchange the "refunding bonds" for the Convertible bonds,* whose funds were used to accomplish this object. The refunding bonds were kept in the treasury of the debtor, which notified the bankers who floated the convertible bonds on the market, that *it would keep the* $45,186,000.00 *Omaha refunding bonds in its treasury* in connection with the issue of the Convertible bonds (R. 4198, Exhibit 3).

Because of these facts, petitioners contended in the District Court that the debtor became *trustee* for the Convertibles. It had no right to pledge these bonds with the Reconstruction Finance Corporation, or, at any rate, the Convertibles were entitled to impress a lien or a trust on the equity in these bonds above the debt due to the Reconstruction Finance Corporation, if the R. F. C. be deemed an innocent party.

It was also urged that by reason of the provisions of the trust indenture securing the Convertible bonds, to the effect that the debtor would insert appropriate provisions for the security of the convertible bonds in the event of the creation of new liens, it became its duty to do so when it acquired the consent from the Commission to issue the refunding bonds, since the lien securing such

bonds commenced only after the permission given by the Commission for their issuance, which was *subsequent* to the sale of the Convertibles. The lien *thereby created constituted a new lien or encumbrance;* as is more fully discussed in the petitions for issuance of writs of certiorari (pages 24-41).

Since the denial of the writs of certiorari on April 19, 1943, there was published in the Advance Sheet of May 1, 1943, the opinion in *Kankakee Federal S. & L. Ass'n* v. *Arnove,* 318 Ill. App. 261, where the Court considered the doctrine of "conventional subrogation." There it said (p. 269):

> "The reason underlying the rule was stated as follows: "This equitable principle is enforced solely for the accomplishment of substantial justice where one has an equity to invoke which cannot injure an innocent person." This principle has been applied when money was advanced to pay off a prior mortgage and a judgment creditor claimed a lien superior to that of the new mortgagee who advanced the money. Citing *Tyrrell* v. *Ward,* 102 Ill. 29."

The Interstate Commerce Commission, which has the primary duty to adopt reorganization plans under §77, treated the Convertibles as unsecured creditors. The issue presented to the District Court on this point was never presented to the Interstate Commerce Commission and escaped its attention. The District Court did consider this issue (35 F. Supp. 230, 254), but under the ruling of this Court it was its duty to refer the matter to the Commission for its consideration. The Circuit Court of Appeals did not consider this issue, as more fully appears from its opinion. The issue was squarely presented to the Circuit Court of Appeals by the statement of points, and argued in the Brief.

This issue is of extreme importance now in view of the fact that it appears from the supplemental record which this Court allowed to be filed simultaneously with the denial of the petitions for certiorari, that the debtor then had on hand over $63,000,000.00 in cash, and the entire debt of the Reconstruction Finance Corporation, in excess of about $48,000,000.00, could now be paid out of the cash so that the debtor could repossess itself of the $45,186,000.00 "Omaha" refunding bonds, and the rights of the convertibles to impress a trust on the "Omaha" bonds or to be subrogated to their lien would place the convertible bondholders in a completely different class.

It also appears from the debtor's petition for rehearing, and from the record attached thereto, that the cash on hand now exceeds $80,000,000.00, and that the debtor has made an application to the District Court for an order directing that the debt to the Reconstruction Finance Corporation be paid. These petitioners have joined in such request, which request was denied by the District Court, but this order is not yet final as it is subject to appeal.

We believe that the payment of the Reconstruction Finance Corporation will not change the structure of the plan. It will not prejudice any of the creditors, but instead will bring them benefits of the savings of interest, and greater participation in debtor's assets and earnings. The approval of the plan prevents the creditors from requiring payment of their claims in advance of the maturities fixed, but should not prevent the reorganized railroad or the Trustee from paying off the debts sooner where the money is available. This should also be done in order to place the Convertibles in the *status quo* so that they may resort to the $45,186,000.00 Omaha bonds and

impress a trust thereon because such bonds were issued for "refunding" and "exchange" purposes and for no other purpose.

The writs of certiorari should, therefore, be issued to preserve the rights of the petitioners and in order to present the entire subject matter to the Interstate Commerce Commission for its due consideration.

II.

The Question of the Reclassification of the Convertible Bonds With General Creditors Was Not Considered By the Interstate Commerce Commission in the Adoption of Its Plan.

The convertible bonds were entitled to 4¾% interest to the maturity of the bond issue and to a premium of 5% plus accrued interest in the event of the retirement prior to maturity. *General creditors were not entitled to such rights.* The Commission treated the Convertible bonds in the same class with general creditors, which cannot be justified under any theory of law.

The provision *to pay interest to maturity of a bond issue is a substantive right* which placed such bondholders in a *different* class from general creditors (*New York Trust Company* v. *Securities and Exchange Commission,* 131 F. 2d, 274, 276). The treatment accorded to the Convertible bonds who were entitled to a premium of 5% plus accrued interest at 4¾% for the retirement of the bonds prior to maturity in the same class with general creditors, *cannot be said to be "fair and equitable"* (*City National Bank & Trust Company* v. *Securities and Exchange Commission,* 134 F. 2d, 65, 66-67). While in the above case the Court justified the action because the

retirement was *involuntary* and it held that the provision was inapplicable to an involuntary retirement, it is applicable here because the appeal was taken from the approval of the plan *prior* to its confirmation, and creditors were entitled to vote upon a "fair and equitable plan."

As stated before, this issue was not presented to the Commission as the petitioners were not parties to such proceedings prior to its adoption of the plan. The issue was presented to the District Court, but the Court evidently failed to note it as it was not even discussed in its opinion. The issue was also not considered by the Circuit Court of Appeals. The subject matter was discussed in the petition for the writs of certiorari under Point II (pp. 22-24).

We are not seeking a rehearing in order to upset the entire plan, but only for the purpose of submitting to the Interstate Commerce Commission these two propositions of fact so that the Convertible bond owners, who were allowed so little participation and whose claim for over $40,000,000.00 was wiped out because of the failure to have these issues and facts presented to the Interstate Commerce Commission, might obtain better treatment.

For the foregoing reasons we urge that a rehearing be granted.

Respectfully submitted,

MEYER ABRAMS,
Counsel for Louis Susman, et al., Convertible Bond Owners, Petitioners.

SHULMAN, SHULMAN & ABRAMS, and
NORMAN ASHER,
134 N. LaSalle Street,
Chicago, Illinois,
Of Counsel.

Certificate of Counsel.

The undersigned, Meyer Abrams, counsel for the petitioners herein hereby certifies that the foregoing petition was prepared by him and that he is of the opinion that the petition is well founded in point of law and is not interposed for purposes of delay.

Dated at Chicago, Illinois, this 10th day of May, A. D. 1943.

Certificate of Service of Copies of Petition on Counsel for Respondents.

I, Meyer Abrams, counsel for the petitioner herein, hereby certify that copies of the foregoing petition were duly served on each of the attorneys of record by mailing printed copies thereof by regular United States mail, postage prepaid on May 10, 1943.

Chicago, Illinois,
May 10, 1943.

MAY 12 1943
CHARLES ELMORE CROPLEY
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM—1942

Nos. 1087, 1088, 1089 62 - 64

In the Matter

of

THE CHICAGO AND NORTH WESTERN RAILWAY COMPANY,
Debtor.

IRVING TRUST COMPANY, as Successor Trustee under the First Mortgage of Milwaukee and State Line Railway Company,
Petitioner,

vs.

MUTUAL SAVINGS BANK GROUP COMMITTEE, LIFE INSURANCE GROUP COMMITTEE, *et al.*,
Respondents.

Petition of Irving Trust Company, as Trustee Under First Mortgage of Milwaukee and State Line Railway Company, for Rehearing and Vacating of Order Denying its Petition for Writ of Certiorari

HAROLD C. MCCOLLOM,
Attorney for Irving Trust Company, as Trustee under First Mortgage of Milwaukee and State Line Railway Company.

Dated, N. Y., May 10, 1943.

APPEAL PRINTING CO., INC., 120 CEDAR ST., NEW YORK, WO 2-3242

IN THE

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MUTUAL SAVINGS BANK GROUP COMMITTEE, LIFE INSURANCE GROUP COMMITTEE, *et al.*,

Respondents.

Petition of Irving Trust Company, as Trustee Under First Mortgage of Milwaukee and State Line Railway Company, for Rehearing and Vacating of Order Denying its Petition for Writ of Certiorari

Irving Trust Company (hereinafter termed the Trustee), as Trustee under First Mortgage of Milwaukee and

State Line Railway Company (hereinafter termed State Line), respectfully applies to this Court, pursuant to Rule XXXIII, for a rehearing and for the vacating of the order made by this Court on April 19, 1943, denying the Trustee's petition for writ of certiorari to the Circuit Court of Appeals for the Seventh Circuit. The opinion of the Circuit Court of Appeals affirming the District Court has now been reported in 126 F. (2d) 351.

Questions Requested to Be Heard

After the filing of this Trustee's petition for certiorari, this Court, on March 15, 1943, rendered its opinions in the *Western Pacific Railroad Company* and *Chicago, Milwaukee, St. Paul & Pacific Railroad Company* cases. While these opinions appear to have disposed of some of the grounds upon which certain petitions for certiorari in the present case were based, they do not dispose of equally important questions raised by this Trustee's certiorari petition; but, on the contrary, they supply strong additional reasons why this Court should determine whether the Circuit Court of Appeals erred by affirming the action of the District Court

(1) in refusing to determine and give effect to the lien of the State Line Mortgage upon the earnings of the mortgaged property;

(2) in giving to the junior mortgages upon the State Line property the benefit of State Line earnings without satisfying the prior lien of the State Line Mortgage;

(3) in basing the treatment of the State Line bonds entirely upon severance studies although there was no possibility of severance;

(4) in confirming a railroad reorganization plan as against a class of bondholders entitled to vote, without the $66\frac{2}{3}$ vote of such class provided for in Section 77(e), merely upon a general determination that the plan is fair and equitable and without making the specific determinations as to the non-assenting class which Section 77(e) requires as a condition of confirmation; and whether

(5) the Circuit Court of Appeals erred in refusing to determine the merits of the objections made by the State Line Trustee.

Grounds of this Petition

1. The Circuit Court of Appeals erred by affirming the action of the District Court in refusing to determine and give effect to the lien of the State Line Mortgage upon the earnings of the mortgaged property.

Certain segregation studies were introduced by the Debtor before the Commission and were stated by the Commission to reflect "as close an approximation as possible to the divisions of joint rates which would have normally been applied if the individual mortgage lines had been separately operated railroads" (R. 3571). Based upon such studies, extended to cover further periods, the Debtor's Comptroller prepared an exhibit (introduced at the hearing before the District Court on confirmation of the plan, R. 5451-5452) from which it appeared that the State Line net earnings (available for interest) for the period from July 1, 1935 (the approximate date of institution of the reorganization proceeding) to April 30, 1941 (the approximate date of the hearing in the District Court on confirmation of the Plan) amounted to $2,424,177. Under the segregation studies the State Line covered its interest requirements by a larger margin than any other

mortgage division (R. 4126-7). It has never been questioned that the State Line Mortgage was a prior lien on the State Line net earnings from the inception of the proceeding. Such earnings amounted almost to the total principal amount ($2,500,000) of the State Line bonds—which matured by their terms on January 1, 1941. No recognition has been given to such earnings either by the Plan or in any other way.

No recognition was given to such earnings in the Plan as transmitted to the District Court and approved and confirmed by it. The Commission recognized the rule of the Seventh Circuit, set forth in the *Wakey* case, that income is impounded for mortgagees by the inception of a bankruptcy proceeding, and said that "there seems no escape from the conclusion that payments out of such funds should be made to the lien holders in the order of their priority" (R. 3669). It refused to consider such earnings in allocating securities under the Plan and stated in substance that the effect of the impounding was a matter for the court (R. 3666). The District Court, by approving and confirming the Plan, also refused to give any weight therein to such earnings; and the Circuit Court of Appeals affirmed.

Nor did the courts below, by means other than the Plan, give any recognition to this lien.[1] If, as is usual in Section 77 cases, the District Court had directed the payment to the State Line bondholders of their net earnings, or a large part thereof, it would not have erred in refusing to give to the bondholders, by the Plan, the bene-

1. Subsequent to the hearing on confirmation the District Court directed certain payments to the State Line bondholders, in common with all other bondholders to which new bonds had been allocated by the Plan; but the amounts of such payments were computed on the basis of earnings applicable on the new securities and were trivial as compared with the impounded net earnings. Except for the last-mentioned payments, the last interest payment on these bonds was made on January 1, 1935 (R. 1773).

fit of the same earnings. However, both the District Court and the Circuit Court of Appeals refused to give any form of benefit to the State Line bondholders. After the first refusal of the District Court to direct any interest payment on the State Line bonds (although by the same order interest payments to other mortgagees were directed), the Trustee appealed to the Circuit Court of Appeals. It dismissed the appeal upon the ground that the District Court's order was not final—even though payments to other mortgagees had been finally directed—inasmuch as the District Court had reserved the power to protect later the State Line rights (114 F. (2d) 963). Having thus been told by the Circuit Court that its remedy was to apply to the District Court for relief, the Trustee several times did so. The District Court continuously refused to consider the matter; and hearing thereon was finally postponed until the date of hearing upon the approval of the Plan (R. 4562). When it approved the Plan it dismissed the application of the Trustee as moot, without any hearing on the merits (R. 5094). The appeals which were decided by the Circuit Court of Appeals (126 F. (2d) 351) included the appeal of the Trustee from the refusal of the District Court to adjudicate and give effect to the lien on earnings; but the Circuit Court's opinion does not mention this matter beyond listing such appeal among the other appeals (126 F. 2d at 353).

At the hearing on approval the District Court, in connection with the impounded earnings contributed by State Line, stated in substance (R. 5018) that such earnings should be calculated on the basis of what the State Line might earn under certain "severance" studies. The severance studies were supported before the Commission and the District Court by an expert for the Group Committees, who testified at the hearing on approval of the

Plan (R. 4358) that one month previously, in the *Wabash Railway Company* receivership case, he had stated that he would not use severance studies to determine the past earnings of a property. Another expert testified at said hearing that such studies can have no effect on past earnings (R. 4133-4). Severance studies, which are intended to estimate earnings under a theoretical future method of operation, cannot be used to determine earnings from actual past operation. No expert testimony is necessary as a basis for such conclusion; but the only testimony in the present case is that just referred to. Independent of the extent to which severance studies may have been used, in other cases, to determine the allocation of new securities, it is the practice in Section 77 proceedings to determine past net earnings by segregation studies; and we believe that in no case other than the present one have severance studies been used for such a purpose.

In the *Western Pacific* case this Court emphasized the necessity for determining and giving effect to mortgage liens. In the *St. Paul* case this Court directed that the cause be remanded to the District Court for the determination, among other things, of the question whether certain properties were covered by the general mortgage or by the 50-year mortgage. The decision of the Circuit Court of Appeals in the present case erroneously approves the action of the Commission and the District Court in destroying the lien of the State Line Mortgage upon earnings of large amount. The State Line bondholders are entitled to the benefit of such earnings, either by way of appropriate changes in the Plan or by way of cash payment.

2. The Circuit Court of Appeals erred by affirming the action of the District Court in giving to the junior mortgages upon the State Line property the benefit of State Line earnings without satisfying the prior lien of the State Line Mortgage.

Although the First and Refunding Mortgage was to a minor extent a beneficiary of the transfer of the State Line's "excess of segregation earnings over final measure of its earnings", the chief beneficiary of such transfer was the General Mortgage. The Plan, while basing its treatment of the State Line bonds upon severance studies alone, gives to the General Mortgage bonds the benefit of most of the segregation earnings of the State Line remaining after deducting the State Line severance earnings. Based upon the segregation earnings for the average depression year used in the calculation, $292,000 of State Line earnings were transferred to the General Mortgage (I.C.C. Ex. 594, p. 8; R. 3249). These State Line earnings (after certain minor modifications) were then used as a part of the base for computing the General Mortgage bondholders' share of new fixed-interest securities, while the severance share of the State Line bondholders was originally $45,000 (I.C.C. Ex. 594, p. 8)—later increased to $51,000 (R. 3244). Similarly, in connection with the allocation of the new income bonds, the same exhibit (later modified in minor respects) for the normal prospective year credited the General Mortgage with $516,000 of State Line segregation earnings (I.C.C. Ex. 594, p. 12).

It was clearly contrary to legal standards and to the requirements of Section 77 that, without satisfying the State Line bonds in full for principal and interest, the Plan should give to the General Mortgage bonds a large

amount of securities by reason of their junior claim upon the State Line segregation earnings while denying to the State Line bonds any benefit from their own segregation earnings. Such treatment is directly contrary to the views expressed by this Court in the *St. Paul* and *Western Pacific* opinions. In the *St. Paul* case, this Court said that the property of one group cannot be "subtly appropriated to pay the claims of another" (87 L. ed. at 713).

3. The Circuit Court of Appeals erred by affirming the action of the District Court in basing the treatment of the State Line Bonds entirely upon severance studies although there was no possibility of severance.

We have noted the language in the *St. Paul* opinion with reference to the use by the Commission of segregation, severance, and contributive income studies, and the holding therein that the studies to be used as a basis for the allocation of new securities are ordinarily matters "for the informed judgment of the Commission and the District Court"; also the holding that the question of the studies to be made is for the Commission "initially" to decide "in the light of the requirements of a particular case" (87 L. ed. at 714). Inasmuch as severance studies have no logical reason for existence in a case wherein severance is a practical impossibility, a question of law is presented as to whether severance studies may properly be used as the sole basis for the treatment of the State Line bonds (if such studies may be used at all) in such a case. The record herein shows that no severance was ever contemplated[2]; that the total reproduction cost less depreciation of the State Line amounted to $3,433,530;[3] that it was

2. R. 3191, 3175-6, 3195.
3. I.C.C. Ex. 217, R. 1608.

built to avoid the very routing which would result from a severance[4]; that operation over the State Line has been highly efficient[5]; that the delay resulting from the theoretical rerouting would be likely to result in the loss of a large amount of the traffic carried[6]; that any proposal to avoid paying $87,500 annual interest to the State Line bondholders by spending a minimum of $1,994,755 (and probably much more)[7] in order to reroute the traffic and recreate the operating conditions which the State Line was built to avoid would be a practical absurdity. Under many decisions of the Commission and of the courts, expenditures for the construction of such a route would not be permitted if any management were insane enough to contemplate so doing. Between the time of the Commisson hearings and the time of the court hearings in the present case the expert who presented the severance studies to the Commission on behalf of the Group Committees testified in another case that severance is entitled to relatively little weight where the possibility of severance is remote (R. 4361).

We are not seeking to reargue any questions decided in the *St. Paul* case. Even if this Court did intend to imply that severance studies designed only to estimate earnings under a theoretical future method of operation may be used, in some cases, as the measure of earning power in spite of the provision in Section 77(e) requiring that due consideration be given to the earning power "past", present and prospective, we do not believe that this Court intended to be understood as approving reorganization allocations based upon severance studies

4. R. 3176, 1639-40.
5. R. 5509, 3190, 4110.
6. R. 1639, 1642, 3149, 3176.
7. I.C.C. Ex. 578, R. 3058, 3124, 3170, 4117-8.

in a case such as the present one, wherein severance would be impossible. Severance studies are extremely speculative and, as used herein, they are revolutionary. If the use of severance studies is to be approved, such use should be carefully restricted. Otherwise, they can be used to destroy investments in divisional mortgage bonds. Such investments are made in the light of the traffic carried over such lines, without any reason to think that the Commission and the District Court—as in the present case—may cut away the position of such bonds by supposing the discontinuance of the efficient line securing such bonds and the substitution of a less efficient new route to be constructed. This is another way of accomplishing the result condemned in the *St. Paul* case—that is, the appropriation of the property of the underlying bondholders.

4. The Circuit Court of Appeals erred by affirming the action of the District Court in confirming a railroad reorganization plan as against a class of bondholders entitled to vote, without the 66-2/3% vote of such class provided for in Section 77(e), merely upon a general determination that the plan is fair and equitable and without making the specific determinations as to the non-assenting class which Section 77(e) requires as a condition of confirmation.

Section 77(e) states that, after the vote of creditors, the Court may confirm the plan if it has been accepted by two-thirds in amount of the allowed claims of each class voting on the plan,

> "*Provided,* That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the

> interests or claims of those rejecting it; *that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts;* and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e); * * *". (Italics supplied by counsel.)

In the *Western Pacific* case this Court said (87 L. ed. at 664) regarding the 1935 amendments to Section 77:

> "* * * While the most important amendment was to furnish means to avoid the obstruction of dissatisfied classes of creditors or stockholders by making a fair and equitable plan effective over dissenters, the requirement of coordinated action by Commission and court was retained."

This language in the *Western Pacific* opinion, combined with denial of certiorari in the present case, may indicate that the so-called "cram-down" provision may be enforced by the District Court merely upon a determination that the Plan is fair and equitable. This would scrap the express proviso in Section 77(e) that the "cram-down" provision may be enforced only if the Court shall also determine that the rejection "is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts". If Section 77(e) is to be thus emasculated, the elaborate and expensive procedure for voting upon a plan is wasted effort, because the initial determination that a plan is fair and equitable would nullify any effect of the voting. We do not believe that this Court intended any such inference to be drawn. The proper interpretation of the proviso above mentioned is novel, is presented to this Court for the first time, and is of great importance in pending railroad reorganizations in which the plans have not been submitted to vote.

The desirability of such an interpretation is emphasized by the particular facts in the present case. 50.37% of the voting State Line bonds were in favor of the Plan and 49.63% opposed. Out of the $1,067,000 of bonds voted in favor of the Plan, $1,000,000 were voted by a member of the Life Insurance Group (R. 5390-3)—which Group was heavily interested in the General Mortgage bonds (R. 5390-3). The Group Committees were largely responsible for the theory under which the State Line's earnings were taken from it and credited to the General Mortgage; and they proposed the allocations which were made by the Commission in the Plan. In spite of this and many other facts, such as those hereinabove mentioned, the District Court paid only lip service to the proviso, recognizing no distinction (so far as anything in the record shows) between the question of whether the plan was fair and equitable and the question of whether the rejection was reasonable. The Circuit Court of Appeals, although it expressed doubt as to the fairness of the Plan to the State Line bondholders and thus gave support to the reasonableness of the rejection, mentioned but did not discuss the matter of reasonableness. In fact, as shown under heading 5 hereof, it refused to consider even the merits of the objections to the Plan. Instead, it criticized the dissenting bondholders and the Trustee for objecting and held in substance that the holder of some $1,000,000 of the $2,500,000 of outstanding State Line bonds—which holder, with other holders,[8] had requested the Trustee to appeal—should accept, without complaint, what the large majority of the system bondholders approved.

8. While the Circuit Court referred to only one bondholder as objecting, the fact was that other bondholders also objected in the District Court (R. 4562-3, 4146-7) and requested the Trustee to appeal.

5. The Circuit Court of Appeals erred in refusing to determine the merits of the objections made by the State Line Trustee.

The objections made by the State Line Trustee and hereinabove mentioned involve questions of law; and they do not depend upon any disputed questions of fact. Nevertheless, the Circuit Court of Appeals refused to determine the merits of such objections, holding in substance that it need not consider such objections, because (a) it must accept the conclusion of the Commission; (b) the holders of other bonds of the system favor the Plan; (c) the holders of a majority of the voting State Line bonds favor the Plan; (d) the objecting bondholders represented only a small percentage of the Debtor's total indebtedness; and (e) the existing position of the objecting bondholders would be bettered because they would be more likely to receive interest and dividends on their new securities.

(As we read the opinion, the Circuit Court may have intended to give the same reasons for not discussing the reasonableness of the rejection of the Plan by the State Line bondholders.)

The Circuit Court stated with reference to the treatment of the State Line bondholders:

> "We confess to the existence of a doubt".

However, it said with reference to such treatment:

> "We must accept the conclusion of the I.C.C. thereon." (126 F. 2d at 370)

Such a holding is contrary to the decisions of this Court in the *St. Paul* and *Western Pacific* cases. In the *Western Pacific* case this Court, although holding that the

decision of the Commission in certain respects is conclusive, said (87 L. ed. at 666) that its determination must be reached "in accordance with legal standards".

The Circuit Court said that it is interested "in the effect of the approval of the plan by the vast majority of the creditors * * * on the various objections which have been raised"; that the voting majority in each group, favoring the plan, was far greater than the two-thirds requirement; that, in respect of those who did not vote, the Court would vote their interest in favor of the plan; that over one-half of the State Line bondholders in volume and number favor the plan; that "one creditor, with a claim of less than one-fourth of one per cent. of the debtor's total indebtedness is attempting to block and defeat the plan"; and that such creditor's position under the plan allocation will be better than its existing position, because its chance of receiving interest and dividends on the new securities will be better (126 F. 2d at 366, 367, 370).

Even if two-thirds of the voting State Line bonds had favored the Plan, the minority were entitled to have the Court comply with the requirements of Section 77; and it would have been error to deprive them "of the benefits of the statute by reason of a waiver, acquiescence or approval by other members of the class" (*St. Paul* opinion —87 L. ed. at 713). *A fortiori,* it was error to treat the rights of the State Line bondholders as affected by the favorable vote of other classes of bondholders.

In so far as the Circuit Court based its refusal to consider the merits of the State Line objections on the small percentage of total system bonds held by the objecting bondholder, such decision is directly opposed to the decision of this Court in the *Los Angeles Lumber Products Company* case, wherein it was held that, upon the "basic

issue'' of the fairness of a plan (under Section 77B), the large percentage of bonds agreeing to the plan was immaterial (308 U. S. at 115), and the plan was sent back upon the objection of less than one per cent. in amount of the bonds.

In so far as the Circuit Court refused to consider the objections because it thought that the objectant would probably receive interest more regularly on the new securities allocated to it, such refusal has no possible justification.

Wherefore, your petitioner respectfully prays reference to its petition for certiorari herein dated March 28, 1942, and respectfully prays that this Court, in respect of the matters above mentioned, grant a rehearing and vacate its order of April 19, 1943 denying this Trustee's petition for certiorari.

Dated at New York, N. Y., this 10th day of May, 1943.

HAROLD C. MCCOLLOM,
Attorney for Irving Trust Company, as Trustee under First Mortgage of Milwaukee and State Line Railway Company.

Certificate of Counsel

I, HAROLD C. MCCOLLOM, attorney herein for the above named petitioner, hereby certify that the foregoing petition was prepared by me and that it is presented in good faith and not for delay.

Dated at New York, N. Y., this 10th day of May, 1943.

Harold C. Mc Collom
HAROLD C. MCCOLLOM